

Nebraska Taxation of Contractors General Information

Effective November, 2005

For more information, check our
Web site: www.revenue.ne.gov



This Information Guide provides an overview of the requirements for contractors regarding the taxation of building materials and their contractor labor. It is not designed to answer all questions that arise, but is intended to enable a person to become familiar with the requirements for operating as a contractor.

Overview

All contractors must collect and remit the appropriate sales tax based on:

- the type of construction project; and
- the contractor option chosen.

Contractors may sell their contractor labor to another contractor tax-free for resale provided they obtain a properly completed Nebraska Resale or Exempt Sale Certificate, Form 13, from the other contractor.

In addition, all contractors must:

- ✓ obtain a Nebraska Sales Tax Permit by filing a Nebraska Tax Application, Form 20;
- ✓ collect and remit Nebraska and applicable local sales and use tax based on the type of construction project and the contractor option chosen; and
- ✓ choose a contractor option by filing a Nebraska Sales and Use Tax Election for Contractors, Form 16.

The contractor option determines two things:

1. how the contractor will pay or collect the tax on building materials and fixtures; and
2. how the contractor will collect the tax from the customer on charges for construction services (e.g. contractor labor).

Definitions

Contractor is any person who repairs property annexed to real estate; or who annexes building materials and fixtures to real estate; or who arranges for such annexation.

Building materials are those items that will become real estate or are annexed to real estate. Examples include lumber, drywall, insulation, and roofing materials.

Building materials do **NOT** include tools, supplies, property, equipment, or other items that will **NOT** be annexed to real estate.

Example: Rebar placed in concrete to reinforce it is a building material. Form lumber to form up the concrete as it is poured is NOT a building material.

Fixtures are items that must be annexed to a building or structure in order to properly function, yet remain identifiable as separate items. Examples include water heaters, furnaces, central air conditioners, and built-in dishwashers.

Unit is any physical portion of a building designated for separate ownership, rental, or occupancy, such as an apartment.

Structure is any construction composed of building materials arranged and fitted together in some way. Structure includes bridges, dams, television towers, fences, sidewalks, decks, billboards, street lighting, waterlines, and water, oil or gas wells.

Construction services means annexing building materials to real estate, including leased property; repair of a structure; or repair of building materials that are, or will be, annexed to real estate.

Construction services also includes the installation, construction, service, or removal of property used in conjunction with the furnishing, installing, or connecting of telephone, telegraph, cable TV, and mobile telecommunications services.

Construction services do **NOT** include the cost of the raw land or finished lot, impact fees, title insurance, property insurance, lender fees, closing costs, inspection fees, real estate brokerage commissions and fees, or any other taxes or fees levied on the transfer of real estate.

Tools, Equipment, Supplies, and Taxable Services

Tools, equipment and supplies are those items used in the completion of a building project that do not become part of the real estate, structure, or fixture. Contractors are the consumers of all tools, equipment, and supplies. Contractors must pay sales tax on tools, equipment, and supplies purchased, rented, or leased for use in completion of a project, including a project for an exempt entity. Examples of taxable tools, equipment, and supplies are hammers, sandpaper, lumber to build forms, office equipment, scaffolding, backhoes, cement mixers, and safety equipment such as barriers, fences, and caution tape.

A contractor's purchases of services, such as building cleaning or maintenance services, pest control services, and security services are taxable. These services cannot be purchased for resale by a contractor.

Contractors must pay sales tax or remit consumer's use tax on the above property and services even on an exempt contractor labor project or on a project performed for an exempt entity. Use tax is commonly due on the purchase or rental of such items and services from out-of-state retailers.

Construction Projects

Charges for construction services (e.g. contractor labor charges) are taxable, unless the project meets one of the six criteria for an exempt labor project listed below:

Exempt Labor Projects

1. The first or original construction of a building or other structure;
2. The addition of an entire room or floor (story) to any existing building;

The addition must increase the square footage of the building, **AND** it must increase the number of rooms or floors in the existing building;

The exemption is limited to the charges associated with:

- the construction of the new room or floor;
 - that part of the existing wall, floor, or ceiling that is altered to accommodate the point of access between the new room or floor and the existing building; and
 - any electrical, plumbing, heating, or cooling system modifications needed to support the new room or floor;
3. The completion of an unfinished portion of an existing building or structure;
 4. The restoration, reconstruction, or replacement of a building or structure damaged or destroyed by fire, flood, tornado, lightning, explosion, ice storm, or natural disaster;
 5. The construction, repair, or annexation of any structure used for the generation, transmission, or distribution of electricity; or
 6. The major renovation of an existing building or unit of an existing building when at least 75 percent of the square footage

of the building or unit is renovated. The exemption must meet the requirements indicated below:

A single renovation project of an existing building or unit of an existing building that involves the rehabilitation, replacement, or reconfiguration of walls or fixtures.

Filing with the department either:

- ✓ a Notification of a Major Renovation Project (applicable **ONLY** to projects on single-family dwellings or duplexes); or
- ✓ an Application for Approval of a Major Renovation.

Notification. The Notification form may be filed **ONLY** for projects on a single-family dwelling or a duplex. It may be submitted by the general contractor, or if there is no general contractor, by the project owner. Upon receipt of a properly completed Notification form, the department will issue an Acknowledgment.

The Notification form may be obtained from the department and is available on the department's Web site.

Application. This form **MAY** be filed for a 75 percent renovation project on a single-family dwelling or duplex along with the required application fee of \$500; and it **MUST** be filed along with the required application fee of \$500 for any construction project that is not a single-family dwelling or duplex.

The Application must be supported by designs, plans, specifications, or other materials, and signed by a licensed architect or engineer indicating the extent of the renovation, the work that is planned to be performed, and the square footage of the floor space that is to be renovated.

The general contractor must keep a copy of the Acknowledgment or approved application to document why sales tax was not collected from the project owner on the contractor labor charges.

Taxable Labor Projects

Projects that **DO NOT** meet one of these criteria are **TAXABLE LABOR PROJECTS**.

Contractor Options

The contractor options apply only to agreements or contracts to:

- annex (attach) building materials to real estate; (e.g. hanging drywall, laying tile, roofing a home)
- repair a structure; or
- repair building materials that are or will be annexed to real estate (e.g. repair a window).

The options **DO NOT** apply to over-the-counter sales.

The options determine two things:

- ✓ how the contractor will pay or collect the tax on building materials and fixtures; and
- ✓ how the contractor will collect the tax from the customer on charges for construction services (e.g. contractor labor).

Option 1. The contractor maintains a tax-free inventory of building materials and fixtures, and may purchase such items tax-free by giving a properly completed Nebraska Resale or Exempt Sale Certificate, Form 13, Section C, block 1 to the supplier.

Option 2. The contractor maintains a tax-paid inventory of building materials and fixtures by paying tax to the supplier at the time of

purchase; or in the case of purchasing such items from an out-of-state supplier, by remitting consumer's use tax.

Option 3. The contractor maintains a tax-free inventory of building materials and fixtures and remits consumer's use tax at the rate in effect at where the items are withdrawn from inventory. The contractor may purchase such items tax-free by giving a properly completed Nebraska Resale or Exempt Sale Certificate, Form 13, Section C, block 1 to the supplier.

A detailed information guide for each option is available on the department's Web site.

Billing the Customer

Contractors must first determine if their customer is another contractor (e.g. subcontractor working for a general contractor), or the project owner.

Billing the Project Owner

When billing the project owner, two criteria determine if sales tax will be collected from the customer:

- 1. the option chosen by the contractor; and
- 2. the type of project - taxable labor project or exempt labor project.

Exempt labor project (e.g. repair of roof damaged by tornado)

■ **Option 1.** The contractor will collect sales tax from the project owner on the total charge for building materials and fixtures.

The contractor will NOT collect sales tax on the charges for construction services (e.g. contractor labor) PROVIDED they are separately stated on the customer's invoice.

If the charges for materials and labor are not separately stated on the customer's invoice, the total charge is taxable.

■ **Option 2 and 3.** The contractor will NOT collect sales tax from the customer on any portion of the bill.

Taxable labor project (e.g. new floor covering installed in existing home)

✓ **Option 1.** The contractor will collect sales tax from the customer on the total charge regardless of how the charges are stated on the customer's invoice.

✓ **Option 2 and 3.** The contractor will collect sales tax from the customer using the appropriate contractor labor percentage to calculate the tax (see "Contractor Labor Percentage" section of this guide).

Contractor Labor Percentage

Option 2 or 3 contractors who are billing the project owner on a taxable labor project **must** use one of four contractor labor percentages to properly calculate the amount subject to sales tax, and the amount of sales tax to be collected from the project owner.

The contractor labor percentage is determined by the sales tax rate in effect at the project site.

Sales Tax Rate	Contractor Labor Percentage
5.5%	57.8%
6.0%	57.6%
6.5%	57.4%
7.0%	57.2%

The contractor labor percentage formula is:

Gross x contractor labor percentage x rate = sales tax to collect from the project owner.

The following example illustrates the contractor labor percentage formula:

An Option 2 or 3 contractor lays new floor covering in an existing home in Lincoln.

Materials	\$6,500.00
Labor	<u>3,500.00</u>
Subtotal (gross)	\$10,000.00
Sales tax	<u>400.40</u>
Total due	\$10,400.40
$\begin{matrix} \$10,000 & \times & .572 & \times & .07 & = & \$400.40 \\ \text{(gross)} & & \text{(contractor} & & \text{rate for} & & \text{sales tax)} \\ & & \text{labor percentage} & & \text{Lincoln)} & & \end{matrix}$	

Labor Only Contracts. On a taxable labor project, Option 1 contractors hired to annex building materials or fixtures owned by another person (labor-only contract) must collect sales tax on the total amount charged.

On a taxable labor project, Option 2 or 3 contractors performing a labor-only contract are required to collect sales tax on the **contractor labor percentage** of the gross receipts.

Billing Another Contractor (e.g. subcontractor billing a general contractor). Contractors may resell their labor (construction services) tax-free to other contractors PROVIDED the billing contractor (e.g. subcontractor) receives a properly completed Form 13, Section C, Block 2, from the buying contractor (e.g. general contractor).

■ **Option 1.** The contractor will NOT collect tax from the general contractor on the labor charges PROVIDED a properly completed Form 13, Section C, Block 2, is received from the general contractor.

The contractor will collect tax from the general contractor on the total charge for building materials and fixtures.

■ **Option 2 and 3.** The contractor will NOT collect tax from the general contractor on any portion of the bill PROVIDED a properly completed Form 13, Section C, Block 2, is received from the general contractor.

Contracts With Exempt Entities

Most nonprofit organizations are **NOT** exempt from sales tax in Nebraska. In addition, not all governmental units are exempt from Nebraska sales tax. The following Nebraska Sales and Use Tax Regulations identify those entities that are exempt from sales and use tax:

- 1-072 United State Government and Federal Corporations;
- 1-090 Nonprofit Organizations;
- 1-091 Religious Organizations;
- 1-092 Educational Institutions; and
- 1-093 Governmental Units.

Contractors performing construction services for entities that are exempt from sales tax must obtain a Purchasing Agent Appointment and Delegation of Authority for Sales an Use Tax, Form 17, from the exempt entity in order to purchase contractor labor, building materials or fixtures tax-free.

The Form 17 **MUST** be obtained **BEFORE** any materials are annexed. The Form 17 may **ONLY** be used for making tax-free purchases of contractor labor, building materials, and/or fixtures that will be annexed to the specific project identified on the Form 17. It may **NOT** be used to purchase or lease tax-free tools, equipment, supplies, or other items that will not be annexed to real estate.

100% Major Renovation — Refund of Tax on Contractor Labor

Renovation projects that increase the market value of a building or unit by at least 100 percent are taxable labor projects, and contractors working for the project owner must collect sales tax from the project owner based on their contractor option.

Project owners may apply to the department for a refund of the sales tax paid to the contractor for contractor labor by filing a Claim for Overpayment of Sales and Use Tax, Form 7.

The refund claim must include sufficient documentation to support the amount of tax paid on contractor labor and the change in market value of the property. Option 1 contractors need to provide their customers separately-stated contractor labor charges.

The method used to determine the market value of the property (by appraisal or assessor's property tax valuation), must be the same both before and after the completion of the project.

Telephone, Telegraph, Cable TV, and Mobile Telecommunications Services

The labor involved to install, construct, service, or remove property used in conjunction with these utility services is taxed in the same manner as contractor labor. The taxation of property used in providing the above services is dependent on whether such property is annexed to real estate or remains tangible personal property after it is installed.

Over-the-Counter Sales

Over-the-counter sales are transactions where the terms of the sales agreement do not require the seller to annex building materials or fixtures to real estate, or to arrange for such annexation.

Example: Customer buys a faucet takes it home and either installs it, or makes arrangements with someone other than the seller to annex it.

Over-the-counter sales also include sales of taxable services such as building cleaning services and pest control services.

Contractors making over-the-counter sales must collect and remit Nebraska and applicable local sales tax on the **total** sales price, including all amounts charged to build or assemble the item sold.

Warranties, Guarantees, Maintenance Agreements, and Service Contracts

Sales of warranties, guarantees, maintenance agreements, and service contracts that cover the repair, cleaning, or maintenance

of buildings or fixtures, or the repair of a structure, are subject to sales tax.

Any building materials used in the performance of such contracts may be purchased tax-free for resale, or may be withdrawn from inventory without incurring a use tax liability.

Sales tax must be collected on parts, materials, labor, or any other charge that is not covered under the agreement. For additional information please see 1-074, Warranties and Guarantees.

Nonresident Contractors

Nonresident contractors have the same tax responsibilities as resident contractors. However, they must also comply with certain registration and bonding requirements (see Nonresident Contractors Information Guide). A nonresident contractor is a contractor who is neither domiciled in, nor maintains a place of business in, Nebraska for more than six months of a year.

General Information

Obtaining a Permit. A Nebraska Sales Tax Permit is obtained by completing and returning a Nebraska Tax Application, Form 20, to the department.

Reporting and Remitting the Tax. Contractors will report and remit the tax on a Nebraska and Local Sales and Use Tax Return, Form 10. In order to properly complete the Form 10, contractors should start with Schedule III which is on the back of Form 10.

Lines 1-15 of Schedule III are used to calculate any difference between gross receipts and the net taxable amount (the amount subject to sales tax).

Lines 16-21 of Schedule III are used to calculate any consumer's use tax a contractor may owe.

Record Keeping. When contractor labor charges are exempt from tax, a copy of the properly completed Form 13 must be kept; otherwise, it will be necessary to keep construction contracts, building permits, bid or building specification, purchase orders, billing invoices, blueprints, drawings, pictures, Department of Revenue acknowledgments or approved applications, and any other documentation that contains sufficient information to accurately describe the construction that was completed.

Taxpayer Assistance. For additional information, please contact the Nebraska Department of Revenue, P.O. Box 94818, Lincoln, NE 68509-4818, or call 800-742-7474 (toll free in NE and IA). In the Lincoln area call 471-5729.